

BEFORE THE IDAHO BOARD OF TAX APPEALS

IN THE MATTER OF THE APPEAL OF IDAHO ) APPEAL NO. 07-A-2218  
YOUTH RANCH NAGEL CENTER, LLC from the ) FINAL DECISION  
decision of the Board of Equalization of Ada County ) AND ORDER  
for tax year 2007. )

**CHARITABLE EXEMPTION APPEAL**

THIS MATTER came on for hearing January 22, 2008 in Boise, Idaho before Hearing Officer Travis VanLith. Board Members Lyle R. Cobbs, David E. Kinghorn, and Linda S. Pike participated in this decision. Attorney Jason Scott, Chief Financial Officer Nancy Proctor, and Board Member Allan Bosch appeared at hearing for Appellant. Deputy Prosecuting Attorney Sherry Morgan appeared for Respondent Ada County. This appeal is taken from a decision of the Ada County Board of Equalization (BOE) denying a charitable exemption for taxing purposes of property described as Parcel No. R7777817790.

**The issue on appeal is whether the subject property qualifies for an exemption from property taxes pursuant to Idaho Code § 63-602C.**

**The decision of the Ada County Board of Equalization is affirmed.**

FINDINGS OF FACT

The total assessed land value is \$4,899,200. Appellant requests subject be granted exemption under Idaho Code § 63-602C as property belonging to a charitable organization.

The subject property is an 8.54 acre parcel improved with warehouse and administrative office facilities. Appellant purchased subject in August 2006 for \$4,600,000.

Appellant detailed the relationship and functions of the entities involved with the subject property: Idaho Youth Ranch, Inc. (IYR), Idaho Youth Ranch Foundation (Foundation), and Idaho Youth Ranch Nagel Center, LLC (Nagel Center).

IYR is a charitable organization formed for the purpose of providing services for the

benefit of troubled children and their families. Most of the 1,800 children helped annually by IYR are referred by the justice system. IYR operates six (6) residential treatment centers in Idaho which deal with drug and alcohol treatment, general residential and long-term care residential treatment, and a shelter home. IYR also provides family services, counseling, and adoption and foster care services. In support of these activities, IYR operates a number of thrift stores (23 currently) throughout the state as a vehicle for converting donations received into cash to fund the treatment centers. Donations from the public come in the form of clothing, furniture, appliances, vehicles, and other items. Funding is also obtained from government contracts and endowments managed by Foundation. IYR is recognized as a charitable organization for federal and state income tax purposes.

Foundation is a § 509(a)(3) support entity formed for the purpose of supporting IYR. Foundation receives certain Board-designated or donor-restricted funds. One such fund rewards children who successfully complete the programs of the IYR with college scholarships. Foundation also manages an endowment fund, which was established for the purpose of making IYR less reliant on swings associated with government contracts.

Until subject was purchased in August 2006, IYR operated a distribution center in Boise. The center was designed to sort, store, and distribute various public donations received by IYR. As the operational demands of the thrift stores exceeded the capacity of the distribution center, the Board of Directors of IYR began exploring options for purchasing a facility suitable for the growth. At that time, IYR became aware of subject.

Subject's prior owner was looking to sell under a 1031 exchange, which meant the window of opportunity to purchase the property was tight. IYR also learned of a federal loan program (New Market Tax Credits) that would allow subject to be financed at a significantly lower interest

rate (4% rather than 6%). To qualify for this program, evaluation of the economic areas surrounding each property owned by IYR would have to be performed. Each property would need to meet the specified qualifications before subject could be purchased under the loan program. As subject's previous owner was looking to quickly transfer the property, evaluation of each property owned by IYR would take too long. Foundation then tried to purchase subject, however, it was found to be ineligible for the program.

To satisfy the requirements of the federal loan program, as well as the desires of the seller, the lending bank suggested the formation of a limited liability company to purchase subject. Nagel Center was then formed, with Foundation as the sole member. It was noted Nagel Center is considered a "disregarded entity" for income tax purposes. The company is not required to file income tax returns. All federal and state income tax consequences are passed directly to Foundation.

The sole purpose of Nagel Center was to own and lease subject to IYR. Under the terms of the triple-net commercial lease, IYR was responsible for all expenses for the property, including; mortgage interest, penalties, and property taxes (if any). Subject is leased to IYR for \$25,000 per month, which equals the monthly mortgage payment. Nagel Center has no employees and is intended to not create a profit.

For 2007, "Idaho Youth Ranch, Inc. and Affiliates" applied on behalf of Nagel Center for property tax exemption as a charitable organization. At BOE the application was denied on the basis Nagel Center is not a charitable entity under Idaho Code § 63-602C. Appeal to this Board followed.

Appellant's arguments concerning the ownership prong of Idaho Code § 63-602C are two-fold. First, the words "belonging to" do not exclude the beneficial owner of the property. Nagel

Center is the owner of record, however, Foundation is the 100% owner of Nagel Center. As such, subject was argued to belong to Foundation because it completely owns Nagel Center. It was contended Nagel Center is merely a shell entity formed for the purpose of securing financing. Further, as Nagel Center is a disregarded entity, the economic “substance” of subject’s purchase should control, not the “form” by which the property was acquired.

Secondly, subject is argued to qualify as property owned by a charitable society. Society was argued to be a group of persons that act together to serve a common purpose. The society in this case being IYR, Foundation, and Nagel Center as legal persons.

Concerning the “use” requirement of the statute, Appellant advocated subject is being used exclusively for the purposes for which Nagel Center was organized. That purpose being to hold title to the property and lease it to IYR, a charitable organization.

Exemption was further argued to be proper if the relevant use is that of the beneficial owner (Foundation). Foundation caused its wholly-owned subsidiary (Nagel Center) to acquire subject and lease it to IYR. Because Foundation’s stated purpose is to support the charitable mission of IYR, Foundation’s “use” of subject (leasing to IYR) purportedly satisfies the use requirement.

The final argument concerning “use” was the charitable use to which subject is put. IYR operates the property as a facility to receive, sort, store, and distribute charitable donations to its thrift stores. The thrift stores sell the merchandise and use the proceeds to fund IYR’s charitable pursuits. IYR is a recognized charitable entity using the subject property for charitable purposes.

Respondent noted exemption statutes are strictly construed against the taxpayer. The relevant statute here requires property be “owned by a charitable corporation or society”. Nagel

Center was created as a limited liability company, which was argued to not be eligible under the plain meaning of the words in the statute.

Further, Nagel Center does not perform the charitable functions. It was created for the sole purpose of holding title and leasing subject to IYR. So while the property is being used exclusively for the purposes for which the organization was established, it was argued those purposes are not charitable. Respondent specifically pointed to the \$100 per day penalties if IYR is late paying the \$25,000 monthly rent. The lease further provides Nagel Center reserves the right to “have and maintain paramount title to the [Property] free and clear of any act or inaction of Tenant [IYR] that may restrict or encumber the [Property].” The terms of the lease agreement were argued to resemble those of a for-profit enterprise.

Additionally, it was contended that while IYR is actually using the property for charitable purposes, the focus is not the use by the tenant, but by the owner. In this case, Nagel Center is the owner using subject as a rental property.

Respondent also argued it was improper to look past Nagel Center as the title holder. The law treats Nagel Center and Foundation as separate legal entities. Respondent further pointed to the Operating Agreement of Nagel Center, particularly the fact that subject does not revert back to Foundation upon dissolution of Nagel Center. Rather, subject would be distributed in accordance with applicable law, which was noted, could include sale to a for-profit third party.

Respondent stated Nagel Center is not part of a society. Referring to Appellant’s definition of society as an association or company of “persons”, Respondent asserted persons do not include limited liability companies or corporations.

Respondent also referenced the eight (8) factors set out by the Idaho Supreme Court in

*Canyon County v. Sunny Ridge Manor, Inc.* to determine the charitable status of a corporation or society and whether the property is used for charitable purposes. Respondent examined each factor and argued Appellant failed to qualify as a charitable corporation or society and the subject property was not used for charitable purposes.

### CONCLUSIONS OF LAW

This Board's goal in its hearings is the acquisition of sufficient, accurate evidence to support a determination of subject's eligibility for property tax exemption. This Board, giving full opportunity for all arguments and having considered all testimony and documentary evidence submitted by the parties in support of their respective positions, hereby enters the following.

Appellant is seeking exemption from property taxation under Idaho Code § 63-602C, which in pertinent part reads, "[t]he following property is exempt from taxation: property belonging to any fraternal, benevolent, or charitable corporation or society . . . used exclusively for the purposes for which such corporation or society is organized."

As noted by both parties, the statute has two (2) elements: the property must belong to a charitable corporation or society and be used exclusively for the charitable purposes for which the charitable entity is organized.

Respondent argued Appellant is not a charitable "corporation or society" as required by the statute. Rather, Nagel Center is a limited liability company and does not qualify under the terms of the statute.

Appellant pointed to a recent act passed by the Idaho legislature amending the language of Idaho Code § 63-602C to include limited liability companies as eligible charitable organizations.

This appeal concerns Appellant's status on January 1, 2007: the applicable assessment

date in this matter. Section 3 of the House Bill referenced by Appellant states “ . . . this act shall be in full force and effect on and after its passage and approval, and retroactively to January 1, 2008.” Accordingly, Nagel Center as a limited liability company, is not eligible for consideration as a charitable entity.

This Board was urged to look past Nagel Center as the record owner of subject and instead qualify the property for exemption because Foundation is the sole member of Nagel Center. Because Nagel Center is a disregarded entity for federal and state income tax purposes, it was reasoned it should be viewed similarly in the property tax arena.

While we agree courts generally disfavor *form over substance* arguments, such is not the case with property tax exemptions.

A statute granting tax exemption cannot be extended by judicial construction so as to create an exemption not specifically authorized. Exemptions are never presumed. The burden is on a claimant to establish clearly a right to exemption. It must be in terms so specific and certain as to leave no room for doubt. *Sunset Memorial Gardens, Inc. v. Idaho State Tax Comm’n*, 80 Idaho 206, 219, 327 P.2d 766, 774 (1958).

Nagel Center is a separately recognized legal entity under Idaho law. Nagel Center’s status as a disregarded entity for income tax purposes has no bearing on its status concerning property taxes. Just as there are benefits of a particular form of business entity, so are there burdens. One must bear the burdens associated with the particular form of entity chosen; even those unintended. Regardless of underlying motivations, Foundation chose to create Nagel Center as a limited liability company. It cannot now chose to ignore this fact to suit the particular situation at hand.

It was argued that while Nagel Center is the record owner of the property, Foundation is the beneficial owner, which should control. We disagree.

“This Court has consistently adhered to the primary canon of statutory construction that where the language of the statute is unambiguous, the clear expressed intent of the legislature must be given effect . . . unless a contrary purpose is clearly indicated, ordinary words will be given their ordinary meaning when construing a statute.” *Corporation of the Presiding Bishop of Church of Jesus Christ of Latter-Day Saints v. Ada County*, 123 Idaho 410, 415, 849 P.2d 83, 86 (1993).

The ordinary meaning of the words “belonging to” is “owner”. In property tax law, the relevant owner is the “record owner”, which is defined in Idaho Code § 63-201(19) as “the person or persons in whose name or names the property stands upon the records of the county recorder’s office.” Nagel Center is undoubtedly the record owner of subject and thus the property belongs to Appellant, not Foundation or IYR. As Nagel Center is not a recognized charitable entity under the law as in effect on January 1, 2007, the subject property is not eligible for exemption under Idaho Code § 63-602C for the 2007 tax year.

Appellant further argued the ownership prong of the test is met because Nagel Center is part of a charitable society along with Foundation and IYR. As society is not defined in Idaho Code, Appellant referenced the leading legal dictionary definition: “[a]n association or company of persons (usu. unincorporated) united by mutual consent, to deliberate, determine, and act jointly for a common purpose.” *Black’s Law Dictionary* 1425 (8th ed. 2004).

Even if we accepted the position that an association of legal entities can form a society, we do not believe Appellant qualifies under the above definition because there is no mutual consent. Foundation is the sole member of Nagel Center and thus controls its activities. Such is spelled out in Section 3.1 of Nagel Center’s Operating Agreement which states “[t]he ordinary and usual decisions concerning the business affairs of [Nagel Center] shall be made by



[Foundation].” There cannot be mutual consent where one entity has full control over the activities of another. If a society exists, it cannot be said Nagel Center is a voluntary member.

Because Nagel Center is not a recognized charitable corporation or society as required by the statute, we need not address whether the subject property is used exclusively for charitable purposes.

We applaud the efforts and charitable intent of IYR, Foundation, and Nagel Center, however under strict statutory construction, subject does not qualify for property tax exemption pursuant to Idaho Code § 63-602C. We understand the reasons why Nagel Center was formed, but unfortunately its formation caused, at least temporarily, unintended property tax liability.

For the reasons above, the decision of the Ada County Board of Equalization is affirmed.

#### FINAL ORDER

In accordance with the foregoing Final Decision, IT IS ORDERED that the decision of the Ada County Board of Equalization concerning the subject parcel be, and the same hereby is, affirmed.

MAILED May 7, 2008